

TENNESSEE GENERAL ASSEMBLY  
FISCAL REVIEW COMMITTEE



**FISCAL NOTE**

**SB 876 - HB 1364**

March 3, 2017

**SUMMARY OF BILL:** Eliminates the sales and use tax on the retail sale of food and food ingredients. Increases the cigarette tax rate from \$0.031 to \$0.0845 per cigarette. Increases the tax rate on all other tobacco products from 6.6 percent to 17.0 percent of the wholesale cost price.

**ESTIMATED FISCAL IMPACT:**

**Decrease State Revenue – Net Impact – \$174,669,500**

**Decrease Local Revenue – Net Impact – \$325,053,900**

Assumptions related to the sales tax on the retail sale of food and food ingredients:

- Based on sales tax collection data from the three most recent fiscal years (FY13-14, FY14-15, and FY15-16), state sales tax collections derived from the retail sale of food and food ingredients are estimated to be approximately seven percent of total state sales tax collections.
- The current Fiscal Review Committee estimate for total state sales tax collections in FY17-18 is \$8,940,000,000.
- The current state sales tax on the retail sale of food and food ingredients rate is 5.0 percent; the average local option sales tax rate is estimated to be 2.5 percent; the effective rate of apportionment to local government pursuant to the state-shared allocation is estimated to be 4.1427 percent.
- Under current law, state sales tax collections derived from the retail sale of food and food ingredients are estimated to be \$625,800,000 in FY17-18 ( $\$8,940,000,000 \times 7.0\%$ ).
- Local revenue pursuant to the state-shared allocation is estimated to be \$25,925,017 ( $\$625,800,000 \times 4.1427\%$ ). Net state revenue is estimated to be \$599,874,983 ( $\$625,800,000 - \$25,925,017$ ).
- Local revenue pursuant to the local option sales tax rate is estimated to be \$312,900,000 [ $(\$625,800,000 / 5.00\%) \times 2.50\%$ ]. Total local revenue is estimated to be \$338,825,017 in FY17-18 ( $\$25,925,017 + \$312,900,000$ ).
- These numbers are assumed to remain constant in subsequent years under current law.
- The recurring decrease in revenue is estimated to be \$599,874,983 for the state and \$338,825,017 for the local government.

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Assumptions related to the cigarette tax:

- Pursuant to Tenn. Code Ann. § 67-4-1004(a) and Tenn. Code Ann. § 67-4-1004(d)(1), cigarette tax is a \$0.62 tax per pack of 20 cigarettes.
- Pursuant to Tenn. Code Ann. § 67-4-1004(b), there is an additional \$0.0005 enforcement and administration fee per pack of 20 cigarettes.
- The total taxes and fees currently imposed are \$0.6205 per pack of 20 cigarettes.
- In FY17-18, under current law, cigarette tax collections are estimated to be approximately \$239,654,664 and additional fee collections are estimated to be approximately \$197,353, for total collections of \$239,852,017 (\$239,654,664 + \$197,353).
- The total number of 20-pack cigarettes sold in FY17-18 is estimated to be 386,546,361 (\$239,852,017 / \$0.6205). This number is assumed to remain constant in subsequent years under current law.
- The average price per pack of 20 cigarettes in Tennessee is estimated to be \$5.00. Increasing the cigarette tax rate by \$1.07 per pack of 20 cigarettes [ $(\$0.0845 - \$0.031) \times 20$ ], for a total tax of \$1.6905 per 20-pack ( $\$0.6205 + \$1.07$ ), is estimated to increase the price of cigarettes to an average of \$6.07 per 20-pack for the consumer. This represents a 21.4 percent increase in the price of cigarettes [ $(\$6.07 - \$5.00) / \$5.00$ ].
- Based on various studies, the price elasticity of demand for cigarettes is estimated to be negative 0.35. The 21.4 percent increase in the price of cigarettes is estimated to result in a 7.49 percent decrease in the quantity of cigarettes consumed ( $21.4\% \times -0.35$ ).
- The number of 20-pack cigarettes sold each year upon passage of this bill is estimated to be 357,594,039 [ $386,546,361 \times (100.00\% - 7.49\%)$ ].
- The total recurring state tax collections upon passage of this bill are estimated to be \$604,512,722 ( $357,594,039 \times \$1.6905$ ). The recurring increase in state tax collections is estimated to be \$364,660,705 ( $\$604,512,722 - \$239,852,017$ ).
- The current state sales tax rate is 7.0 percent; the average local option sales tax rate is estimated to be 2.5 percent; the effective rate of apportionment to local government pursuant to the state-shared allocation is estimated to be 3.617 percent.
- The total taxable sales of cigarettes are expected to increase by \$237,864,009 as a result of this bill [ $(357,594,039 \times \$6.07) - (386,546,361 \times \$5.00)$ ].
- The recurring increase in state sales tax revenue is estimated to be \$16,048,233 [ $(\$237,864,009 \times 7.0\%) - (\$237,864,009 \times 7.0\% \times 3.617\%)$ ].
- The total recurring increase in local sales tax revenue is estimated to be \$6,548,848 [ $(\$237,864,009 \times 2.5\%) + (\$237,864,009 \times 7.0\% \times 3.617\%)$ ].
- The total recurring increase in state revenue is estimated to be \$380,708,938 ( $\$364,660,705 + \$16,048,233$ ).

Assumptions related to other tobacco products:

- Pursuant to Tenn. Code Ann. § 67-4-1005, the tax rate on all other tobacco products, including cigars, is 6.6 percent of the wholesale cost price.

- In FY17-18, under current law, tax collections from sales of other tobacco products are estimated to be approximately \$18,073,000. Taxable sales under current law are estimated to be \$273,833,333 ( $\$18,073,000 / 6.6\%$ ). This number is assumed to remain constant in subsequent years under current law.
- Based on information provided by the Department of Revenue, wholesale purchases of other tobacco products are estimated to decrease by 3.61 percent as a result of the tax rate increase to 17.0 percent.
- The recurring taxable sales are estimated to be \$263,947,950 [ $\$273,833,333 \times (1 - 3.61\%)$ ]. The recurring state tax collections are estimated to be \$44,871,152 ( $\$263,947,950 \times 17.0\%$ ).
- The recurring increase in state revenue is estimated to be \$26,798,152 ( $\$44,871,152 - \$18,073,000$ ).

Assumptions related to the net impact of this bill:

- The net recurring decrease in state revenue is estimated to be \$192,367,893 ( $\$599,874,983 - \$380,708,938 - \$26,798,152$ ).
- The net recurring decrease in local revenue is estimated to be \$332,276,169 ( $\$338,825,017 - \$6,548,848$ ).
- Fifty percent of tax savings will be spent in the economy on non-food sales-taxable goods and services. Fifty percent of additional tax spending would have been spent under current law in the economy on non-food sales-taxable goods and services.
- The net impact of this bill is tax savings of \$524,644,062 ( $\$192,367,893 + \$332,276,169$ ). Fifty percent of this amount, or \$262,322,031, will be spent in the economy on non-food sales taxable goods and services.
- The current state sales tax rate levied on non-food sales-taxable goods and services is 7.0 percent; the average local option sales tax rate is estimated to be 2.5 percent; the effective rate of apportionment to local government pursuant to the state-shared allocation is estimated to be 3.617 percent.
- The net recurring increase in state sales tax revenue as a result of 50 percent of tax savings being spent in the economy on non-food sales-taxable goods and services is estimated to be \$17,698,369 [ $(\$262,322,031 \times 7.0\%) - (\$262,322,031 \times 7.0\% \times 3.617\%)$ ].
- The total recurring increase in local revenue as a result of 50 percent of tax savings being spent in the economy on non-food sales-taxable goods and services is estimated to be \$7,222,224 [ $(\$262,322,031 \times 2.5\%) + (\$262,322,031 \times 7.0\% \times 3.617\%)$ ].
- The net recurring decrease in state revenue as a result of this bill is estimated to be \$174,669,524 ( $\$192,367,893 - \$17,698,369$ ).
- The net recurring decrease in local revenue as a result of this bill is estimated to be \$325,053,945 ( $\$332,276,169 - \$7,222,224$ ).

**CERTIFICATION:**

The information contained herein is true and correct to the best of my knowledge.

A handwritten signature in dark ink that reads "Krista M. Lee" followed by "RNC" in smaller letters.

Krista M. Lee, Executive Director

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